Supreme Court, U.S.
FILED

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No.

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM 1997

TOTAL FOODS; THOMPSON CANDY; NABISCO BRANDS, INC.; UNITED DISTRIBUTIVE WORKERS COUNCIL 30, RWDSU AFL-CIO; DUANE WILSON & ASSOCIATES; JOHN ROEHRIG; and SANDERS CONFECTIONERY PRODUCTS, INC.,
Petitioners,

v.

JAY ALIX, Individually and as Trustee,
Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

PETITION FOR WRIT OF CERTIORARI

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40 pp

QUESTIONS PRESENTED FOR REVIEW

1. Can the disclosure of conflict of interest under 11 USC 101(14) and 11 USC 327(a) be precluded or waived under any "preclusive" doctrines.

2. Can a conflict of interest under bankruptcy law be waived by 'acquiescence" or inaction of the parties and not be disclosed to the Court.

PARTIES TO THE PROCEEDING

1. All parties to the proceeding in the court whose judgment is sought to be reviewed are included in the caption of the case.

2. There are no parent companies or nonwholly owned subsidiaries.

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OPINIONS BELOW

The opinion of the United States Court of Appeals for the 6th Circuit in Total Foods, et al. v. Jay Alix is included below as Appendix A.

JURISDICTION

The judgment of the United States Court of Appeals was rendered November 12, 1997. The jurisdiction of this Court is invoked under the provisions of 28 U.S.C.§1254(1).

INTRODUCTION

The United States Bankruptcy Code provides in 11 USC 101(14) and 11 USC 327(a) that the professionals, including the Trustee, are required to be "disinterested", defines the requirements of "disinterested", then requires the professional to file the relevant disclosure form with the Bankruptcy Court. In the instant case it was undisputed that the Trustee Jay Alix was required to file a disclosure for himself but failed to do so. Also, when he filed the disclosure for his accounting firm, he failed to disclose that he as the named owner had a conflict of interest.[1] Inter alia, the conflict of interest specifically arose from a written agreement between Jay Alix, the Trustee, and the CEO of the Debtor's corporation

The Jay Alix case reads like a John Grisham novel and

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1 Alix would have been disqualified under 11 USC § 101(14), particularly subsection (E) which provides in part " . . . does not have an interest materially adverse. . . .by reason of any direct or indirect relationship . . . or for any other reason"

parallels the recent case of the federal conviction of the New York based Milbank Tweed lawyer John Gellene last week for failure to disclose his conflict of interest in a Wisconsin based bankruptcy case to the presiding bankruptcy judge.

As the result of Jay Alix being able to avoid disclosing his conflict of interest, he and his accounting firm realized approximately $1,000,000 in fees with more pending and achieved national prominence that he would not have otherwise been able to do without the offices of this trusteeship.

The political environment existing in the Detroit Bankruptcy Court at the time was that the new bankruptcy judge assigned to the case, fearing that the 28 plus adversary cases filed in the Debtor's bankruptcy would be effected, avoided hearing the merits of the case to remove the Trustee. The Sixth Circuit held that the doctrine of res judicata prevented a hearing on the merits of the conflict of interest of the Trustee. The doctrine of res judicata was predicated upon the faulty premise in the District Court that the confirmation of the plan in bankruptcy prevented hearing any challenges to the Trustee's actions. The Bankruptcy Court held that this also precluded holding a hearing on the merits of the disqualification and removal of Jay Alix. The bankruptcy case has now been going on for ten years since the plan was confirmed with active participation of the Trustee in some 28 adversary proceedings. The Trustee's intentional concealment of his conflict in interest, which was not discovered until eight months after the Plan was confirmed, has been barred from any hearings under the theory of res judicata.

The Bankruptcy Court held the case for more than five (5) years, avoiding rendering an opinion for years on end, and then claimed the case was precluded for not being timely

brought.

Under the Bankruptcy Code an action can be brought at any time to remove a trustee for cause. Otherwise, it would give a trustee or other professional virtual immunity for any conduct. Preclusive doctrines are never permitted to prevent review of professional misconduct. That was never the intended result of the bankruptcy code.

The District Court and the Sixth Circuit used a false factual concept to invoke the preclusive doctrine of res judicata to avoid hearing the case that Counsel was never able to correct. There were never any hearings on the merits of the allegations that Jay Alix had an undisclosed conflict of interest and had in fact, never filed a disclosure. In fact the Bankruptcy Court held that the neither Jay Alix nor his accounting firm had filed a proper disclosure, and but for res judicata created by the confirmation of the plan he could be removed. Instead he was allowed to serve for eight additional years with immunity for all subsequent conduct and obtain fees for himself and his accounting firm in excess of $1,000,000.

There is no legal distinction between a professional and officer of the court to make a written disclosure and omit to disclose a conflict of interest (or lack of disinterest) and the professional making no disclosure because any disclosure would reveal a conflict of interest (lack of disinterest). The proper legal terminology is misfeasance versus nonfeasance.

The first issue has now presented itself with national prominence against the New York law firm of Milbank, Tweed in the form of a criminal conviction in Milwaukee, Wisconsin against Milbank Attorney Gellene. The factual side of the story is reported in a January 23, 1998 Wall Street

Journal article attached to this as Appendix C at A14. The Federal indictment against Attorney Gellene is attached as Appendix B at A9. While the facts in this case may vary from the instant case, the statutory and case law is the same. It also illustrates this case has issues affecting national jurisprudence and that it is appropriate for this Court to review.

The gravamen of the federal indictment is that when the Milbank Tweed Attorney Gellene filled out the bankruptcy representation forms to comply with the mandatory disclosure of "disinterest" he omitted to disclose that his firm had prior representation of a creditor that formed a conflict of interest for him and the law firm participating in the bankruptcy of the Debtor. Since the disclosures were a written document, the failure to disclose this information was a criminal offense under 18 USC 152 and 18 USC 1623. Attorney John Gellene has been convicted in Milwaukee, Wisconsin, the situs of the Debtor's bankruptcy. Milbank Tweed has already made arrangements to return $1.9 Million in fees.

Both the Milbank Tweed case in Milwaukee, Wisconsin and the Jay Alix case from Detroit, Michigan are extremely egregious examples of professional misconduct, which the legal system has not cured.[2]

The principals of the Debtor, Filipp Kreissl and John Sanders relied upon Alix disclosing his prior conflict of

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2 The Clerk of the Milwaukee District Court where the indictment is pending reports requests for information from all over the country on this case. The issue is not just confined to this isolated Milbanks Tweed case nor to the instant Jay Alix case. Where there is a lot of money to be made people will find ways to circumvent the rules.

interest and assumed the Court had approved it The Sixth Circuit is saying that since Kreissl and Sanders did not oppose Jay Alix's appointment before confirmation, the issue can not be raised after confirmation of the plan Jay Alix was excused from failing to comply with 11 USC 101(14) and the sanctions of 18 USC 152 and 18 USC 1623. Attorney John Gellene was convicted for the same egregious conflicts of interest that Jay Alix is being excused from because of procedural technicalities.

To add further injury Jay Alix was appointed as the only lay person to the National Bankruptcy Review Commission of 1994 to suggest revisions to the United States Bankruptcy Code. One of the main revisions being considered was that dealing with the employment of professionals and the modification of the rules dealing with 11 USC 101(14) concerning the issue of disinterest of professionals in Chapter 11 bankruptcies. Obviously it was in Jay Alix's best interests while serving on the Commission to get the bankruptcy code changed.

In the instant situation Fred Sanders Inc. was forced into a Chapter 11 Bankruptcy by Heller Financial Inc. As part of the underlying agreement which was later repudiated by Heller, Heller told Sanders management that if they filed Chapter 11, Heller would continue to fund. Heller then forced the appointment of Alix as Trustee even though there was a long history of animosity between the Debtor's CEO and Alix that would have disqualified Alix under 11 USC 101(14).

Heller Financial Inc. temporarily continued funding but threatened the creditors committee that if they objected to Jay Alix's appointment, Heller would stop funding and cause the business immediate financial ruination. It was assumed that Alix had filed a disclosure of some type with the Court

that was approved by the Court. When it was discovered that the actions of Heller were fraudulent and that Alix never filed a disclosure, this action was filed.

Alix filed disclosures for his professionals but never filed any disclosure for himself. If he had filed a truthful disclosure he would have been disqualified from functioning as the Trustee in one of the largest high profile bankruptcy cases in the history of Detroit and would have missed out on a $1 Million dollar fee.

This case is one that affects the national jurisprudence. There has been no other case this Court has heard addressing the "lack of disinterest" requirements of a trustee or what the court's responsibility is to insure the integrity of the judicial system in this sort of matter.

STATEMENT OF THE CASE

The debtor in this case, Fred Sanders, Inc., a 115-year-old confectionery institution in Detroit, was forced to file for protection under Chapter 11 on November 16, 1987 (Case No. 87-06979, Bankr. E.D. Mich. Nov. 16, 1987), when its commercial lender, Heller Financial,, Inc., filed an action to foreclose its commercial line of credit and existing loan without notice.

On December 4, 1987, Heller filed a motion for appointment of Jay Alix as operating trustee, exerting financial duress to not object to the appointment of Jay Alix despite an otherwise disqualifying conflict of interest with management.

The Bankruptcy Court and the District Court do not dispute that the Trustee did not have a "lack of disinterest"

but rather was the timing right to hear a challenge to the appointment of Jay Alix. The time never runs on a fraudulent concealment.

Several years before, Alix had been employed in a management firm, KWD Group, which was owned by Kreissl , the Chief Executive Officer of the Debtor Fred Sanders Inc.. The employment relationship between Alix and Kreissl became very hostile and litigation was avoided in 1984 through a formal written settlement agreement obtained through mediation between the parties, which, inter alia, barred the parties from speaking negatively about each other or discussing either party's business activities with employees of that party in perpetuity. There were other instances of barred conduct between the parties.

Alix did not conceal his animosity and even said to a member of the Creditors Committee that "I would work for nothing, if I could get even with Kreissl" (the Debtor's CEO).

While Alix's lack of disinterestedness became known to various parties to the bankruptcy, no one knew that Alix had failed to file a disclosure statement. The assumption was that despite his open animosity he filed a disclosure as required by statute and it had been approved by the Court.

After Alix's failure to disclose became known in late 1988, the Debtor's parent company, Sanders Confectionery Products, Inc. (SCPI) filed a motion to remove the trustee in Bankruptcy Court on February 7, 1989. The SCPI motion was filed eight months after the Order of Confirmation, not the two years mistakenly stated in the ruling of the Court of Appeals for the Sixth Circuit which gave rise to this petition.

Eventually, the majority of the members of the Creditors Committee either filed similar motions to that of SCPI or joined the existing motions. This included Detroit Edison Company, chair of the committee, which filed a motion in behalf of all creditors.

On the same day, February 7, 1989, SCPI, its officers and a shareholder seeking certification as a class, filed a 13-count lawsuit against Heller, its attorney and Alix (Sanders Confectionery Products, Inc. et al v. Heller Financial, Inc. et al, 973 F2d 474, 480 (6th Cir. 1992) ("Sanders") alleging, inter alia, conspiracy, fraud on the Bankruptcy Court, lender liability, securities violations and RICO violations. The case was filed in the District Court on a basis of subject matter jurisdiction and included a request for jury trial.

The Bankruptcy Court denied a hearing on the merits of the disqualification of Jay Alix in its Opinion dated April 8, 1994. The Court opined, however, that "theoretically the confirmation of the plan was irrelevant to whether claims alleging the trustee's failure to disclose a potential conflict of interest can be raised" and "11 U.S.C. §1141 does not foreclose bringing an action against a trustee after confirmation" and "11 U.S.C. §322(d) does not support the idea that confirmation of a plan relieves a trustee from liability because that section provides for actions on a trustee's bond for up to two years after a trustee is discharged."

That being said, the Court then declared that the motions to remove Alix filed in the Bankruptcy Court were res judicata to the decision in the "Sanders" District Court case. The Court admitted that it was apparent that neither Alix nor his own accounting firm had filed the necessary disclosures.

REASONS FOR GRANTING OF THE WRIT

It is in the interest of the national jurisprudence for this Court to issue a position on what the responsibilities of the Court and the professionals are in a bankruptcy action with regard to professional responsibility and the "disinterest" requirement.

This is not a case concerning whether the District Court and the Sixth Circuit were correct in their precise holding whether the objections to Jay Alix's conflict of interest were timely made.

What is of concern to jurisprudence is that the court system went to great efforts to avoid hearing very egregious conflicts of interest in order to preserve all the judicial work done in an extraordinarily long bankruptcy case in Detroit. This was wrong and is a total abuse of the legal system. This is best exemplified by the efforts in Milwaukee Wisconsin in the Milbank Tweed case and the subsequent federal conviction of attorney Gellene to restore integrity to the bench and bar.

The Bankruptcy Court decision was affirmed upon appeal to the U. S. District Court and by the Court of Appeals for the Sixth Circuit in its ruling on November 12, 1997 which gives rise to this petition.

ARGUMENT

The plaintiffs in this matter assert that the issue involved is not so much Alix's conflict of interest and bias, as serious as that may be, but rather Alix's intentional effort, with reckless disregard to conceal this lack of disinterestedness by failing to file a disclosure statement. This

is a direct attack on the integrity of the Bankruptcy Court and to the judicial system itself.

Alix's deliberate failure to file a disclosure statement, a matter of strict liability, stands in sharp contrast to his 1994 appointment to the National Bankruptcy Review Commission. The appointment was, in fact, a cruel irony, coming at the time when the various motions to remove him were finally being dealt with by the Bankruptcy Court, albeit without hearing on the merits.

Alix's appointment in this bankruptcy had profound consequences to 800 creditors, who have not received one penny, while Alix and his accounting firm have been paid over $1,000,000, with an additional $250,000 pending. Three thousand shareholders of SCPI, the parent corporation of the Debtor lost their investment less than one year after making it.

In addressing the issue of Alix's removal, all three of the Courts put emphasis on the lack of timely objection to his appointment; that is, prior to the Order of Confirmation. The failure to disclose was not barred by confirmation of the plan. A fraud concealed is never barred by any .ype of statute of limitations nor any other preclusive doctrines.

Any suggestion that silence and the forbearance to object represented a waiver by the parties is off-set by the circumstances.

- First, as mentioned above, these parties assumed that disclosure had been made but that the appointment had been approved by the Court nevertheless. This, of course, did not turn out to the be case. No disclosure has been made to date.

- Second, while the parties had become aware of the conflict of interest and bias, they did not know that Alix had not filed the disclosure statement and had thus deprived the Bankruptcy Court of its right to rule on Alix's disinterestedness. This is the issue here, and it is both a legal and moral one.

- Further, the members of the Creditors Committee, who knew of the conflict of interest and bias, were under enormous duress from Heller, which made it clear that any challenge to Alix would be met with a cessation of funding.

CONCLUSION

But the fundamental point here is that the trustee's responsibility to perform (i.e., file a disclosure) cannot be waived by the silence of other parties.

Respectfully submitted,

Richard L. Roble JD,PC

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Dated: March 11, 1998

APPENDIX

APPENDIX A

Filed November 12, 1997

No. 96-1816

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FORTHE EASTERN DISTRICT OF MICHIGAN SOUTHERN DIVISION

In re FRED SANDERS, INC., Debtor.

TOTAL FOODS; THOMPSON CANDY; NABISCO BRANDS, INC; UNITED DISTRIBUTIVE WORKERS COUNCIL 30, RWDSU AFL-CIO; DUANE WILSON & ASSOCIATES; JOHN ROEHRIG; and SANDERS CONFCTIONERY PRODUCTS, INC.,

Plaintiffs-Appellants,

v.

JAY ALIX, Individually and as Trustee,

Defendant - Appellee.

BEFORE: MARTIN, Chief Judge; RYAN and BATCHELDER, Circuit Judges.

PER CURIAM. Plaintiffs appeal the order of the district court affirming the bankruptcy court's dismissal of the motion to replace the trustee in the bankruptcy proceedings of Fred Sanders, Inc. For the reasons that follow, we AFFIRM the order of the district court.

I.

Debtor, Fred Sanders, Inc. ("FSI"), filed a petition for protection under Chapter 11 of the Bankruptcy Code on November 16, 1987 (hereinafter "bankruptcy proceeding"), after its major creditor, Heller Financial Services, Inc. ("Heller"), foreclosed on its loans. Contemporaneously with the filing of the petition, FSI moved for the appointment of an examiner. Apparently, defendant Jay Alix was suggested for this function, but when creditors objected, Alix was not named. On December 4, 1987, Alix was appointed operating trustee in the Chapter 11 proceedings. The record reflects no objections to his appointment, and no appeal was taken from the order appointing him.

On May 4, 1987, the bankruptcy court entered an order confirming the plan of reorganization. No appeal was taken from this order.

On February 6, 1989, almost two years after entry of

the order confirming the plan, two things happened. First a collection of creditors and interested parties filed a suit in federal court against Heller, Alix and others. The action was entitled *Sanders Confectionery Products, Inc. v. Heller Financial,* 973 F.2d 474 (6th Cir. 1992) (hereinafter *Sanders*) The *Sanders* complaint alleged lender liability, fraud, securities violations, RICP violations, and conspiracy. The complaint made vague reference to the claim that Alix was not "disinterested" and therefore should not have been appointed trustee, but did not seek Alix's removal as trustee. Second, and also on February 6, 1989, Sanders Confectionery Products, Inc.; the parent company of the debtor and an unsecured creditor in the bankruptcy proceedings, filed a motion in those proceedings to have Alix replaced as trustee, claiming that Alix was not disinterested and had failed to disclose his interest to the bankruptcy court.

Heller opposed the motion filed in the bankruptcy proceedings and filed a motion in *Sanders* to withdraw the reference to the bankruptcy court of the Fred Sanders, Inc. bankruptcy proceedings for the limited purpose of deciding the motion to replace the trustee. Eventually, the district court, without mentioning the motion to withdraw the reference, dismissed all of the plaintiffs' claims in *Sanders* on res judicata grounds, holding that each of those claims was barred by the final order of the bankruptcy court confirming

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The motion to withdraw the reference was denied by the district court shortly after the court issued its opinion dismissing the complaint.

the FSI Chapter 11 plan. We affirmed that judgment. Thereafter, the bankruptcy court dismissed on res judicata grounds the motion to replace Alix as trustee. The district court affirmed that judgment, holding that the order of confirmation in the Chapter 11 proceedings barred the motion, and noting in a footnote that the judgment in *Sanders* precluded the motion as well. This timely appeal followed.

The essence of the motion to replace Jay Alix as trustee is the movants' claim that Alix was not eligible to be appointed trustee because he was not disinterested as required by the Bankruptcy Code, and he had failed to disclose this fact to parties to the bankruptcy proceedings and the bankruptcy court. Alix's alleged interest stems from his prior relationship with Filipp Kreissl, the president of both FSI and FSI's parent company, Sanders Confectionery Products, Inc. ("SCPI"). Prior to 1984, Alix worked for Kreissl in a non-related accounting consulting company known as KWD Group, Inc. While employed by Kreissl, Alix did limited work for FSI. Alix and Kreissl had a falling out; Alix either resigned or was fired; a lawsuit resulted, and the suit was settled.

The record reveals that Filipp Kreissl knew about the

We did not affirm the district court's judgment of res judicata s to the claims of one shareholder, concluding that this particular shareholder was not in privity to the parties whose claims were adjudicated, but dismissed that shareholder's claims as having been improperly pled. This single exception to the res judicata bar is not material to the analysis before us in the instant case.

Alix's relationship with Heller is also vaguely alleged as an interest. The record indicates that multiple parties knew about his relationship at the onset of Alix's appointment.

alleged interest. It is undisputed that prior to being appointed trustee, Alix was suggested for appointment as examiner in the Chapter 11 proceedings and Kreissl objected to the appointment because of Alix's past relationship to Kreissl. In addition, affidavits submitted in support of the motion to replace Alix reveal that other creditors and interested parties knew about the trustee's interest early in the bankruptcy proceedings. In her affidavit, the Secretary-Treasurer of the union which represented FSI employees states that in a meeting "held shortly after the appointment of Alix as trustee" Alix said, "I would work for nothing, if I could get even with Fil Kreissl." Another affiant, John Schamante, a creditor and a member of the Creditors committee in FSI's bankruptcy, makes it clear that the Creditors' committee knew about the trustee's interest early in the bankruptcy proceedings. According to Schamante's affidavit, the Creditors Committee discussed in meetings held" [s]hortly after Mr. Alix's appointment ....." Alix's relationships with and attitudes toward various parties to the bankruptcy proceeding. Despite this early knowledge of Alix's alleged interest, no party chose to object to Alix's appointment or more for his removal in a timely manner.

II

"It is well settled that in an appeal from a district court's review of a bankruptcy court's decision, this court directly and independently reviews the bankruptcy court's decision. This court applies a plenary review of the bankruptcy court's conclusions of law, using a *de novo* standard.

In re Eagle Picher Indus., 999 F.2d 969 (6th Cir. 1993) (citations omitted).

III

In order for an action to be barred by res judicata, four elements must be satisfied. Those elements include:

1. A final decision on the merits in [a prior] action by a court of competent jurisdiction;

2. The second action involves the same parties, or their privies, as the first;

3. the second action raises an issue actually litigated or which should have been litigated in the first action;

4. An identity of the causes of action. *Sanders Confectionery Products, Inc. v. Heller Financial*, 973 F2d 474, 480 (6th Cir. 1992). Each of these elements is present here.

1. A Final Decision On the Merits

In *Sanders*, this court held that an order confirming a Chapter 11 plan is a final order for the purposes of res judicata. *Id.* at 480. We affirmed the district court's order dismissing that case on res judicata grounds based on the bankruptcy court's order of confirmation of the Chapter 11 plan in the FSI bankruptcy. Further, we held that all claims against the trustee in the FSI bankruptcy proceedings related to his conduct during that bankruptcy should be considered

core proceedings, and that the final order of confirmation operated to bar subsequent core proceedings. *Id.* at 483, n.4. The bankruptcy court then held that the motion to replace the trustee in the FSI bankruptcy proceedings raised exactly the same issue relative to the trustee as had been raised in *Sanders,* and denied the motion on res judicata grounds. Thus, for purposes of the appeal before us, it is immaterial whether the final decision on the merits in a prior action is determined to be the judgment in *Sanders* or the final order of confirmation in the bankruptcy proceedings. Either will suffice.

2. Same Parties Or Their Privies.

This element is not contested by the appellants. In any event, this court clearly held in *Sanders* that creditors and equity security holders of the debtor must be considered to be parties to the bankruptcy proceedings for res judicata purposes. *Sanders,* 973 F.2d at 480. We further held that both Sanders Confectionery Products, Inc. and Alix were parties to the FSI bankruptcy proceedings. *Id.* at 481. The appellants here are all creditors who joined in SCPI's motion in the bankruptcy proceedings to replace the trustee or filed similar motions of their own. The bankruptcy court, relying on the language of our discussion in *Sanders,* expressly found that SCPI adequately represented the interests of the other movants seeking to replace the trustee. In addition, SCPI was one of the plaintiffs in the *Sanders* case. Although the parties to this motion and *Sanders* are not exactly the same, we conclude that the bankruptcy court and the district court correctly held that the second element required for a finding of res judicata is present.

3. Issues Which Were, Or Should Have Been Litigated In First Action.

A full reading of the record reveals that most, if not all, of the parties to the bankruptcy proceedings knew about Alix's alleged interest early in those proceedings. The record belies any contention to the contrary. The issue of interest could and should have been raised prior to the confirmation of FSI's Chapter 11 plan. This element of the res judicata analysis clearly has been met.

4. An Identity Of The Causes Of Action.

"Identity of causes of action means an 'identity of the facts creating the right of action and of the evidence necessary to sustain each action.' " *Sanders*, 973F.2d at 484 (quoting Westwood Chemical Co. v. Kulick, 656 F2d 1224, 1227 (6th Cir. 1981). the facts and evidence supporting the motion to replace the trustee are identical to the facts and evidence necessary to prove the allegations raised in *Sanders* that Alix failed to disclose that he was not disinterested and that he had acted contrary to the interest of the estate. Furthermore, it is clear that these facts and this evidence were available to the parties prior to the confirmation of the Chapter 11 plan. The fourth element is clearly present.

The order of the district court affirming the order of the bankruptcy court dismissing the motion to replace the trustee is **AFFIRMED**.

Dated: November 12, 1997

APPENDIX B

Case No. 97-Cr-221

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF WISCONSIN

UNITED STATES OF AMERICA,
Plaintiff,

v.

JOHN GELLENE,
Defendant.

INDICTMENT

THE GRAND JURY CHARGES:

Allegations Common to All Counts

1. Bucyrus-Erie Company, a mining equipment manufacturer, filed bankruptcy in the Eastern District of Wisconsin, on February 18, 1994. Also filing bankruptcy was the related corporate entity, B-E Holdings, Inc.

2. Creditors of Bucyrus-Erie included: (a) Goldman, Sachs, & Co.; (b) Jackson National Life Insurance Company; and (c) a group of investment entities known as South Street Funds.

3. South Street Funds was managed and directed

by Greycliff Partners. Greycliff Partners consisted of Mikael Salovaara and Alfred Eckert, former employees of Goldman, Sachs, & Co.

4. In contemplation of filing bankruptcy, Bucyrus-Erie Company retained the services of the New York law firm, Milbank, Tweed, Hadley & McCloy (hereafter "Milbank Tweed").

5. After the bankruptcy was filed, the legal representation of Bucyrus-Erie, as well as the compensation of the lawyers, was subject to court approval.

6. A dispute in the bankruptcy concerned lawsuits and potential lawsuits among Bucyrus-Erie; Jackson National Life; Goldman, Sachs & Co.; Michael Salovaara; Greycliff Partners; and South Street Funds arising from financial transactions preceding the bankruptcy.

7. An additional material matter was the connection of Milbank Tweed to the debtors, creditors and other parties in interest in the bankruptcy.

8. John G. Gellene was the lead attorney at Milbank Tweed in the bankruptcy representation of Bucyrus-Erie.

COUNT ONE

THE GRAND JURY FURTHER CHARGES:

1. On or about February 18, 1994, in the State

and Eastern District of Wisconsin and elsewhere,

John G. Gellene,

did knowingly and fraudulently make a false material declaration in the bankruptcy case of Bucyrus-Erie.

2. The false declaration was made under penalty of perjury (as permitted by federal law) and was submitted in support of Milbank Tweed's application to be approved as bankruptcy counsel for Bucyrus-Erie.

3. The declaration was submitted under Bankruptcy Rule 2014, which required Gellene to state all of Milbank Tweed's connections with the debtors, creditors, and any other party in interest.

4. The declaration was false because Gellene knowingly failed to state that Milbank Tweed represented Salovaara, Greycliff and South Street Funds.

All in violation of Title 18, United States Code, section 152.

COUNT TWO

THE GRAND JURY FURTHER CHARGES:

1. On or about March 28, 1994, in the State and Eastern District of Wisconsin and elsewhere,

John G. Gellene,

did knowingly and fraudulently make a false material declaration in the bankruptcy case of Bucyrus-Erie.

2. The false declaration was made under penalty of perjury (as permitted by federal law) and was submitted in support of Milbank Tweed's application to be approved as bankruptcy counsel for Bucyrus-Erie.

3. The declaration was submitted under Bankruptcy Rule 2014, which required Gellene to state all of Milbank Tweed's connections with the debtors, creditors, and any other party in interest.

4. The declaration was false because Gellene knowingly failed to state that Milbank Tweed represented Salovaara, Greycliff and South Street Funds.

All in violation of Title 18, United States Code, section 152.

COUNT THREE

THE GRAND JURY FURTHER CHARGES:

1. On or about November 29, 1995, in the State and Eastern District of Wisconsin,

John G. Gellene,

while under oath, did use a document knowing that the document contained a false material declaration.

2. The document was the declaration signed by Gellene on March 28, 1994, which stated, in part:

> Besides the representations disclosed in my declaration dated February 18, 1994, after due inquiry I am unaware of any other current representation by Milbank of any equity security holder or institutional creditor of the Debtors.

3. The declaration was false because Gellene was aware and knowingly failed to state that Milbank Tweed represented Greycliff and South Street Funds.

4. Gellene used the document during his testimony at a bankruptcy hearing that included a dispute over whether Milbank Tweed should receive approximately $2 million in attorneys fees.

All in violation of Title 18, United States code, section 1623.

A TRUE BILL:

/s/_____ _____
Frank Klein, FOREPERSON
Dated: 12/9/97

/s/_____
Barbara B. Berman for
Thomas P. Schneider
United States Attorney

APPENDIX C

The Wall Street Journal
Friday, January 23, 1998

INSIDE A WHITE-SHOE LAW FIRM'S CONFLICT CASE

By Paul M. Barrett

The prominent New York law firm Milbank, Tweed, Hadley & McCloy has tried to blame an embarrassing conflict of interest problem entirely on John Gellene, a quirky ex-partner who faces criminal charges of misleading a bankruptcy court in Milwaukee.

But there is more to the story that one man's foibles.

The conflict involves clients of a far more celebrated Milbank lawyer: Lawrence Lederman, a titan of the takeover wars in the late 1980s who quite Wachtell, Lipton, Rosen & Katz because it opposed his plan to publish a memoir. The episode provides an unusual glimpse at the inner workings of a blue-chip firm and how it has dealt with potentially explosive conflict-of-interest allegations.

When Mr. Lederman joined Milbank in 1991, some incumbents at the old-line firm worried that he would bring with him conflict-of-interest difficulties. But his reputation and client list were enticing to a firm that was worried about slipping from the profession's top rank. Mr. Lederman became head of Milbank's M & A practice, one of the firm's

top billers and one of its best-paid members.

Six years later, though, the conflict fears came true. Milbank last month agreed to repay $1.9 million in fees after issuing a rare public apology for keeping secret its simultaneous representation of Lederman clients Bucyrus International, Inc. and financier Mikael Salovaara. Mr. Salovaara's investment funds were creditors in Bucyrus's bankruptcy proceedings in Milwaukee in 1994. Milbank still faces a malpractice suit, filed jointly by ex-client Bucyrus and another former creditor, who trace the potential for compromised loyalty to Mr. Lederman.

Depositions of Milbank lawyers reveal that Mr. Lederman, now 62, let it be known within the firm that he didn't see a problem with the dual representation. Mr. Gellene, who became an M & A lawyer in 1996, agreed with the man who headed the department. Messrs. Lederman and Gellene have declined to comment. Milbank's outside lawyer, William Conlon, says, "The firm believes Larry Lederman was absolutely ethical at every step, but otherwise, the firm believes it would be inappropriate to comment at this time."

So far, only Mr. Gellene faces criminal punishment, because he is the one who allegedly covered up the dual representation in bankruptcy court. But legal ethics scholar Monroe Freedman of Hofstra University sees a broader problem at 375-lawyer Milbank and other large firms that he contends don't vigorously police potential conflicts among their many clients.

"Why Milbank hasn't gotten the message is amazing,"

says Prof. Freedman, pointing to a separate 1994 case in which a federal appeals court in New York upheld a $2 million jury verdict against Milbank stemming from a former client's conflict-of-interest claims.

The Bucyrus bankruptcy judge, Russell Eisenberg, seems similarly concerned. Milbank "knows how to do things correctly," he said at a hearing in Milwaukee last month. "Was somebody asleep on the job? Did somebody in charge not care?"

The seeds of this mess were sown in 1991, when Milbank's executive committee urged the admission of Mr. Lederman to energize the firm's anemic M &A practice. His aggressive style and variety of clients would "undoubtedly increase the number" of potential conflicts at Milbank, but those situations would be closely monitored, the Milbank committee told the other partners in a memorandum. The memo added that "he is a lucid thinker and writer, although sometimes difficult to understand orally because he goes too fast for the comprehension of others." (Mr. Conlon, Milbank's outside lawyer, says, "The considerations about Larry Lederman joining the firm were absolutely standard.")

Among those on Mr. Lederman's client list were Bucyrus, a maker of mining equipment, and Mr. Salovaara, a "vulture" investor known for buying securities of distressed companies. Mr. Salovaara, 43, has long stirred controversy by using his investments in ailing companies to gain advantage in their restructurings. Brainy and well-versed in bankruptcy law, he left a partnership at Goldman, Sachs & Co. in 1991 after the investment banking firm scrapped his vulture fund

there in response to criticism from Goldman clients.

Milbank expected to represent Mr. Salovaara's funds "in all investment where we have no conflicts," the Milbank executive-committee memo said. In December, 1991, Mr. Lederman became one of Milbank's top-paid partners, drawing more than $1 million a year.

In 1992, Mr. Lederman did the legal work for a $35 million high-interest loan to Bucyrus from Salovaara-controlled funds. This was the fourth Bucyrus financing Messrs. Lederman and Salovaara had helped orchestrate, beginning with the company's leveraged buyout in 1988, according to Bucyrus. While Mr. Lederman's juggling of relationships with Bucyrus and Mr. Salovaara didn't yet cause a formal conflict problem, some attorneys say they would have avoided taking on both clients.

In early 1993, Bucyrus defaulted on its debt, creating yet more business for Mr. Lederman. He introduced the company to Mr. Gellene for restructuring or Chapter 11 bankruptcy reorganization.

Mr. Gellene, now 41, soft-spoken but intense, was well enough respected that the firm had forgiven him for a bizarre lapse. In 1989, Milbank discovered that the Harvard Law graduate had passed the New York bar exam but had never undergone a required interview, thus practicing without a law license for nine years. Mr. Gellene said in a deposition last October that during the 1980's,he "simply suppressed the matter from his day-to-day awareness." He left the firm temporarily, obtained his bar card, and was readmitted in

1990 as a full partner.

The Bucyrus restructuring quickly turned ugly. Another major creditor, Jackson National Life Insurance co., wanted Bucyrus to pursue fraud claims against Mr. Salovaara for the financings that had buried the company in debt. Mr. Gellene advised against pursuing such claims. In fact, he said Mr. Salovaara should receive a formal release from liability.

Jackson, based in Lansing, Michigan, sued Mr. Salovaara on its own. "We were really scratching our heads over why Milbank wasn't going after Salovaara," says Andrew Rahl, Jackson's outside lawyer.

Mr. Gellene represented Bucyrus but checked in periodically with Mr. Lederman, who remained the billing partner. In the summer of 1993, when Bucyrus asked to have a pending $415,000 bill itemized, it was Mr. Lederman who refused. "The all-consuming nature of this project and the 'round-the-clock availability of our lawyers should be all the backup that you require," he wrote the company. Bucyrus paid the bill.

While the restructuring attempt continued, Mr. Lederman began representing Mr. Salovaara in a dispute with his partner in the very same vulture funds that were creditors of Bucyrus. Between late 1993 and mid-1994, Milbank attorneys recorded 880 hours on the Salovaara case.

Mr. Lederman and Mr. Salovaara were also keeping up a social relationship. In 1993, they attended a bicycling camp together, and they shared Thanksgiving dinner, Mr.

Salovaara has testified.

Back at Milbank's Wall Street offices, at least one attorney was worried about a conflict. Litigation partner Toni Lichstein, who was involved in both cases, aired her concern during a meeting in Mr. Lederman's office in December 1993. Mr. Lederman responded that "he didn't see it as a problem, because the matters were unrelated," Ms. Lichstein said in a deposition last September. Mr. Gellene, who was also at the meeting, agreed that "there was no issue," Ms. Lichstein recalled.

Mr. Gellene recalled the incident in his deposition, remembering that Mr. Lederman said Mr. Salovaara wanted Milbank's representation of him kept "confidential." Mr. Salovaara and Milbank have since strongly denied this.

Mr. Lederman said in his deposition last September that he didn't recall the meeting at all. Asked if he had circulated a routine "new case" memo to make sure there wouldn't be any conflicts with the Salovaara representation, he said he didn't recall, adding: "I don't really do those kinds of administrative things. Somebody would do it." (A memo was circulated, Mr. Conlon, the outside lawyer, says.)

When Bucyrus slid into Chapter 11 proceedings in February 1994, the U. S. Trustee in Milwaukee raised questions about whether Milbank had adequately disclosed any potential conflicts to the judge. Mr. Gellene made two formal conflict disclosures in 1994, but neither mentioned the Salovaara work. He also failed to disclose that Milbank had begun to represent Salovaara funds in the acquisition of debt

of a broadcasting company - a separate project which Mr. Gellene himself supervised.

Mr. Gellene said in his deposition that in February, 1994 he reiterated to Mr. Lederman that he didn't plan to disclose the Salovaara connection. "Mr. Lederman acknowledged what he heard and said nothing that led me to believe that he disagreed with anything I said or my analysis," Mr. Gellene recalled. Mr. Conlon says that Mr. Lederman didn't play a role in the Bucyrus Chapter 11 case.

Ms. Lichstein, who was handling litigation chores in both the Salovaara partnership case and the Bucyrus chapter 11, was still worried, however. In April 1994, she met separately with Messrs. Gellene and Lederman to discuss the conflict issue, and was told again not to fret. But Mr. Lederman added that if the dual representation made her "uncomfortable," Milbank would bow out of the Salovaara partnership dispute, according to the Lederman deposition. The firm withdrew in June.

In late 1994, Mr. Lederman wrote off $325,000 in Milbank bills to Mr. Salovaara. A December 1994 internal memo explained that Mr. Lederman saw the representation as unsuccessful but expected other "significant business" from Salovaara, some of which was already under way.

Bucyrus emerged from Chapter 11 in late 1994, with Jackson still pressing its fraud suit against Mr. Salovaara, some of which was already under way.

Then, in late 1996, John Stark, general counsel of a

Jackson affiliate, was leafing through court papers during a plane ride when he stumbled on references to Mr. Lederman's representation of the financier in the dispute with his vulture-fund partner. "I nearly fell out of my seat," Mr. Stark recalls.

Bucyrus, under new management, demanded its $1.9 million in fees back, echoing Jackson's accusation that Milbank may have treated Mr. Salovaara too gently in the bankruptcy case, at the expense of Bucyrus and other creditors.

Last April, Milbank made its unusual apology to the bankruptcy court for not disclosing the situation. But the firm blamed the failure entirely on Mr. Gellene and demanded to keep its $1.9 million in fees on the theory that no actual harm had occurred.

Put on paid leave while under psychiatric care, Mr. Gellene accepted full responsibility. The father of three small children, he believed the firm would stand by him, as it had in the bar-admission episode, according to a person familiar with the situation.

He was wrong. A federal investigation started in early 1997, and Mr. Gellene was expelled from the firm in November, then indicted. Milbank fought furiously to keep its fees, but in December, it repaid them to avoid a bankruptcy-court hearing in which Mr. Gellene would have been the star witness.

In a possible foreshadowing of his defense at a trial set

for next month, Mr. Gellene said in a bankruptcy-court filing in December that he had been kept in the dark about the extent of Mr. Salovaara's relationships with Mr. Lederman and Bucyrus, and that he might have been more vigilant if he had known all the facts.

A Tangle of Clients

Key events in the Milbank Tweed conflict of interest case:

1988: Lawrence Lederman and Mikael Salovaara advise Bucyrus International buyout group tin deal that leaves company with heavy debt.

1991: Lederman represents Salovaara in connection with his withdrawal from Goldman Sachs.

Lederman leaves Wachtell Lipton to Join Milbank; brings Bucyrus and Salovaara with him as expected clients.

1992: Lederman advises Bucyrus on taking $35 million high interest loan from Salovaara controlled funds.

1993: Bucyrus defaults. Lederman brings Milbank the lucrative assignment of restructuring Bucyrus, and asks Milbank partner John Gellene to handle day-to-day chores.

Bucyrus creditor Jackson National Life Insurance accuses Salovaara of defrauding Bucyrus. Milbank declines to pursue these claims. Jackson sues Salovaara on its own.

Lederman simultaneously begins representing Salovaara in separate dispute with his investment fund partner.

1994: Bucyrus begins Chapter 11 process.

Lederman agrees to back out of Salovaara representation.

Jackson discovers simultaneous representation.

1997: Bucyrus demands return of $1.9 million in fees from Milbank.

Gellene expelled by Milbank, indicted by federal grand jury in Milwaukee.

Milbank agrees to return the $1.9 million; still faces $100 million malpractice suit filed by Jackson and Bucyrus.